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Im Fokus

The Free Trade Agreement Negotiations between Japan and Chile: Causes for Reaching a Rapid Agreement

Die chilenisch-japanischen Verhandlungen zu einem Freihandelsabkommen: Die Gründe für eine schnelle Übereinkunft

Leslie Wehner

Abstract

The present article analyses the internal and external factors that facilitated the reaching of a rapid agreement between Japan and Chile after five rounds of Free Trade Agreement (FTA) negotiations. The issue area of agriculture dominated the FTA agenda because of Japanese unwillingness to make many concessions in its previous FTAs and because of Chile's comparative advantages on this issue. Therefore, this FTA negotiation was expected to be time-consuming. However the attainment of a final agreement within ten months surprised even the most optimistic groups with stakes in the negotiation. I argue that internal as well as external factors to the negotiation are important to understand not only the negotiated outcome but also the attainment of such a rapid agreement.

Keywords: FTA, Chile, Japan, agriculture, negotiation

Introduction

The former Prime Minister of Japan Shinzō Abe and the President of Chile Michelle Bachelet signed a joint declaration on September 3rd, 2007 in Tokyo, with which the Free Trade Agreement (FTA) between both countries formally started (XNA, 4/9/07). The formal negotiations were conducted in five rounds from February to November 2006 and the final agreement was signed on March 27th, 2007. Despite initial concerns on whether an agreement was possible and achievable in the short term, the fast pace of the negotiations and the attainment of a final agreement within ten months surprised even the most optimistic groups with stakes in the negotiation. The concern over whether an FTA was possible were due to the sensitivity of the issue areas that both countries presented during

the meetings of the joint working groups created in 2001 and then in 2005 to analyse the plausibility of having an FTA.

On one hand, Chile has comparative advantages in the agricultural sector, in which Japan has been unwilling to make many concessions in its other bilateral FTA negotiations. On the other hand, Japan has comparative advantages in some of Chile's sensitive areas, for example the production of metal products such as iron, steel and aluminium. However, the main problems of the negotiation were on the Japanese side, specifically on the issue areas of agriculture along with seafood and dairy products.

The Japanese executive has been extremely responsive to the demands of agricultural groups in its FTA negotiations. These demands are often channelled through the political representatives of the ruling Liberal Democratic Party (LDP) elected with the support of agricultural sectors – *nōrin zoku*. Hence, the Japanese government, in the hands of the LDP, was also aware of the possible electoral impact in its agricultural sector support if painful concessions were made during negotiations (Yoshimatsu 2006: 482). Agriculture was thus the main impediment to reaching a final agreement, even before the formal negotiations started, because the Japanese perceived Chile as a country heavily dependent on agriculture. What factors facilitated such a rapid agreement between these two countries despite the existence of such sensitive issue areas in the negotiation? This question is what guides the present article.

The aim of this article is to provide an exploratory analysis of the negotiation process and the negotiated outcome in relation to the agricultural sector as well as the internal and external aspects that facilitated a rapid agreement. Even though I refer to both countries' economic policies, the main focus lies on Japan's bilateral FTA strategy. To answer the question posed in this article, first, I provide an overview of the antecedents of the pre-negotiation. Second, I analyse the negotiation process as such, i.e. the strategies used by both countries over the agricultural sector and issue areas as metal products that to some extent help to explain the rapid agreement. Third, I discuss some factors external to the negotiation that facilitated the start and the conclusion of this process. These external factors are mainly the extant agreements that Chile has with China, the European Union (EU), South Korea and the United States (US), which are Japan's direct competitors in the global economy. Finally, I provide a brief overview of the outcome of the negotiation as a whole, beyond the agriculture issue area, i.e. the scope of the FTA.

Antecedents of the Pre-negotiation

The idea of having an FTA between these two parties can be traced back to 1999, when the Chilean Minister of Foreign Affairs proposed to the Chairman of the Japanese External Trade Organisation (JETRO) the establishment of a working group to analyse the plausibility of having an FTA. This working group was established in May 2000 and the final report was published in 2001. The report highlighted the benefits that an FTA would bring to both parties, although it also suggested that careful attention would need to be paid to sensitive issue areas on both sides i.e. agriculture for Japan and some industrial goods such as some steel and iron products, as well as some electro-domestic products in the case of Chile. "[...] we conclude that the maximum effort should be made to conclude an FTA between Japan and Chile as soon as possible" (JETRO 2001: 27).

Despite the willingness of export producers and the respective Ministries of Foreign Affairs to launch an FTA negotiation, this only occurred in November 2005 during the Asia-Pacific Economic Cooperation (APEC) meeting in South Korea. Here both parties agreed to start formal negotiations during the following year. This official announcement was based on the results of a new Joint Study Group Report that analysed for a second time the plausibility of having an FTA. This latter group was established in 2004 and its final report came out the same month in which the launch of formal negotiations was announced by the then Japanese Prime Minister Jun'ichirō Koizumi and the then Chilean President Ricardo Lagos (MOFA 2005a).

The second working group concluded that an FTA was possible and desirable to enhance both parties' respective trade positions in Latin America and Asia. According to the official report of this working group, an eventual FTA would increase Japan's exports to Chile by 42 percent (USD 290 million), whereas Chile's exports to Japan would increase by 15 percent (USD 380 million). In the same text, both parties highlight their respective concerns on their sensitive areas that were the same products that were mentioned in the First Joint Working Group Report in 2001. Therefore, both countries agreed on analysing eventual exclusions of certain products from the final agreement, on a case by case base (MOFA 2005b: 5, 11-13).

The Negotiation Process

The rapid agreement reached in five rounds can be attributed, to some extent,

to the negotiation process as such. Japan used a mixed strategy in the FTA negotiation. A mixed strategy presents elements of distributive as well as integrative bargaining used either sequentially or simultaneously (Odell 2000). On the areas of low conflict, the negotiation strategy was integrative or joint-problem-solving and allowed the complete removal of the six percent tariff for Japanese autos in the Chilean market, and the gradual removal of the three percent tariff on Chilean copper (*Business Asia* 2007). However, in the agricultural issue area, Japan mainly used a defensive distributive strategy, which is expressed in its initial willingness to exclude a broad range of products from the deal.¹

Japan's defensive distributive variant was accompanied by some concessions over products that were already signalled as negotiable during the formal negotiations. Some of these negotiable products were pork, chicken and beef meat, as well as some fruits such as apples, grapes, and grapefruits. Low tariff quotes were assigned to the former products and transition periods from 10 to 15 years to the latter (MOFA 2007: Annex 1). These offers and counteroffers were referred to both countries' domestic constituencies for ratification during the formal negotiation in the so-called "next room" (Direcon-Prochile 2006a, 2006b, 2006c). Yet Japan made sure these concessions would be given to Chile only if the exclusion of its key sensitive products was assured such as rice, wheat, oranges, mandarins, dairy products and plywood. These products were finally excluded from the agreement. In addition, many fish and clams products were also excluded, yet the main concern for Chile was to assure the inclusion of salmon in the agreement. Finally, salmon was included but with a progressive removal of tariffs over ten years (MOFA 2007: Annex 1, pp. 133-269).

The success of Japan's ^{issue} negotiation strategy can be explained by an extant asymmetrical economic dependence that favoured Japan. The expected

¹ A negotiating strategy can be classified as distributive (value-claiming) or integrative (value-creating). On one hand, a distributive strategy is "[...] a set of actions that promote the attainment of one party's goals when they are in conflict with those of the other party". On the other hand, an integrative strategy "[...] involves actions that promote the attainment of goals that are not in fundamental conflict – actions designed to expand rather than split the pie" (Odell 2000: 31-34). In real terms a negotiation as a whole involves a mixed strategy combining both value-claiming and value-creating strategies. However, in some issue areas of FTA negotiations it is possible to observe the predominance of one of the two strategies. A defensive variant of distributive strategy is used to prevent the opposition taking value from one's own sensitive issue areas.

economic impact of the FTA shows that Japan's GDP would only increase by 0.002 percent, while Chile's GDP would increase by 0.49 percent (MOFA 2005b: 5). In addition, Japan is Chile's third most important trade partner (Libertad y Desarrollo 2007: 2), while imports from Chile represented less than one percent of Japan's total imports in 2006 (Direcon-Prochile 2007). Therefore, Chile needed the FTA agreement more than did Japan. This fact played a major role during the negotiation because it gave Japan more leverage to protect its sensitive agricultural products vis-à-vis the demands of Chile over the different issue areas of the negotiation.

The success of Japan's negotiation strategy in protecting key agricultural products can also be attributed to the fact that Japan signalled to Chile at the very outset of the negotiation the non-negotiability of issues such as rice, dairy products, wheat, oranges, mandarins, apple juice and plywood. This signalling of non-negotiability started during the meetings of the Joint Study Group and is reflected in the way its final report, published in 2005, is written with regards to the agricultural sector.

The Japanese side insisted that as the products mentioned before are sensitive due to political and economic reasons, regardless of whether or not Chile can export them or has specific interests in them, exclusion of sensitive products from the coverage of trade liberalization under a Japan-Chile EPA/FTA would be appropriate. (MOFA 2005b: 13)

During the formal negotiations, Japan increased its signalling that there was no possibility of talking on the aforementioned sensitive issues. Whenever Chile tried to bring up these issues Japan refused to discuss them. Finally, Chile ceased to insist on them. A proof of this is that the Chilean association of food producers complained before the last round of negotiations that some agricultural and sugar products were not even discussed during the previous rounds (*Diario Financiero* 2006). Yet, the Japanese strategy of non-negotiability of specific products always went along with a commitment to reach agreements over other issue areas, such as salmon, other type of fruits, and juices, as a compensatory measure to assure the reaching of a final agreement.

Third, when Japan decided to pursue a defensive variant of a distributive strategy, it tacitly allowed its counterpart to claim the exclusion of some of its most sensitive issues. The most important exclusions for Chile were some flat-rolled products of iron and non-alloy steel of different sizes; as well, Chile got some favourable transition periods – ten to twelve years – for removing

the extant six percent tariff on other steel products. In addition, Chile also excluded from the agreement structures, bars, rods and profiles of aluminium. Chile could also exclude sensitive footwear products like ski-boots, while other type of footwear with an extant six percent tariff will be progressively phased out in ten to twelve years time (MOFA 2007: Annex 1, pp. 383, 395, 411).

Japan's defensive distributive strategy was reciprocated by Chile, following a tit for tat strategy. Nevertheless Chile used a more integrative strategy during the negotiation since Chile's trade as a whole depends more on Japan than the inverse. Japan's Best Alternative to a Negotiated Agreement (BATNA)² was better than Chile's one. Japan used its BATNA as a tactic to get its sensitive agricultural issues excluded from the agreement. Yet Japan was committed to finding a zone of agreement because external factors such as trade diversion effects posed problems for its auto exporters.

Finally, Japan's interest in having an FTA was mainly based on the idea of assuring free tariff access for its auto producers as well as the supply of Chilean copper that was going to China, due to the high demand and the already existing FTA between Chile and China. This fact facilitated the negotiation process because the parties expected maximal benefits in low conflict issue areas, i.e. autos and copper. Therefore, all other benefits beyond these issue areas were seen as complementary. In fact the trade pattern between Chile and Japan is dominated by these two issues. More than 50 percent of Chilean exports to Japan are copper and other minerals like molybdenum (The Pacific Institute Studies 2006: 23), whereas motor vehicles are Japan's main source of exportation to Chile (*Business Asia* 2007). Even though Japan will progressively phase out the extant three percent tariff on purified copper in ten years time, other copper products got immediate free tariff accesses such as copper mates, cement copper, unprocessed copper, copper bars, copper rods and copper profiles as well as some refined copper products like wire-bars (MOFA 2007: Annex 1, pp. 408-409). Nevertheless an FTA negotiation is about maximising benefits in all possible economic sectors. Yet the assurance of the two most important issue areas of the negotiation facilitated the acceptance of delimited exclusions of products from the agricultural issue, and it also allowed for the inclusion of other issue areas in which trade could be created.

² BATNA is the status-quo ante, another FTA negotiation or the unilateral removal of some tariffs.

External Factors that Facilitated the Negotiation

Chile showed flexibility in accommodating Japan's interests over agricultural issues during the negotiation because Chile knew what had been negotiated in Japan's previous FTAs, specially with Mexico. In this regard, Chile claimed concessions to get low tariff quotas as Mexico did on products like pork, beef and chicken meat, but it did not strongly insist on claiming the inclusion of agricultural products that were excluded from the agreement with Mexico. This predisposition of Chile to accommodate Japan's claims on agriculture were plausible because the cost of an eventual stalemate were higher for Chile than for Japan. However, Japan and Chile both knew that the non-agreement option would be mutually painful because of the trade diversion effect created by the extant trade agreements that both countries had.

Japan made it clear to potential trade partners that agriculture would be protected during any FTA negotiation. The best example is the first FTA that Japan signed in January 2002 with Singapore, whose agricultural sector did not pose any real threat to Japan's agricultural producers. Nevertheless, Japan used its first FTA to establish a blueprint for its future trade partners on what was possible to negotiate and what was not (Dent 2005: 306), as well as to show how difficult it would be to claim concessions in the agriculture issue area without jeopardising the success of the negotiation as a whole. A similar pattern of negotiation on agriculture was followed with Mexico (Corning 2007: 50). Despite Japan giving Mexico some concessions in its less sensitive agricultural products through non-renegotiable low tariff quotas and transition periods of 5, 7, 10, 12 and 15 years, the core of sensitive products, such as rice, wheat, apples, tangerines and dairy products, were excluded from the agreement (Foreign Press Center Japan 2004).

This second negotiation with a Latin American country was simplified in many ways by Chile's pragmatic negotiation strategies with its other trade partners. When Chile negotiated with a country for which agricultural issues were extremely sensitive, it opted to accept the exemption of some of these products to assure the reaching of a final agreement. This pragmatic policy set a precedent for other potential trade partners who are likely to demand the same benefits conceded by Chile in its other FTAs. Japan followed a similar negotiation pattern to those used by Korea and China during their negotiations with Chile over agricultural products. In fact, these three countries managed to

exclude some similar agricultural products in their negotiation with Chile, and postpone the negotiation of certain products for the future as Table 1 shows.

Table 1 Sensitive Products Excluded from FTAs with Chile

JAPAN	CHINA	KOREA
rice, wheat, dairy products*, oranges**, mandarins**, apple juice, certain sugar products and plywood	rice, wheat, wheat flour, iodine, urea, and certain wood products	rice, pears, apples, dairy products***, onions***, mandarins***, oranges***, and strawberries***

Remarks: * To be negotiated after two years once the agreement is implemented

** To be negotiated after five years once the agreement is implemented

*** To be negotiated once an agreement is reached at the WTO negotiations.

Sources: MOFA 2007: Attachments, 133-269; Direcon 2006: 23, 2003: Annexe 3.4, Appendix 2, section C.

Even though Japan proposed to negotiate dairy products in two years time as a way to respond to its domestic groups and to Chile's pressure on this issue, a future outcome that removes the extant trade barriers either totally or partially is not at all certain. The reasons are that the real commitment and the pressure to find a mutually satisfactory agreement in a future negotiation over dairy products, oranges and mandarins as well as eventual renegotiations of some other agricultural products is eliminated once the FTA is implemented.³ Moreover, the negotiation already set up a clear precedent that Japan will negotiate these residual issues using a distributive strategy as it did in the current FTA.

Whereas Chile is considered one of the FTA champions in the global economy, it is also true that its pragmatic approach to FTAs and excessive flexibility have tied its hands on what it can claim, and on what it has to concede vis-à-vis its negotiating counterparts to assure an outcome of agreement.

Another important external factor that facilitated the agreement was the FTAs that Chile already had with Japan's main trade competitors in the global economy. Chile has FTAs with the EU, the US, South Korea and China. Richard Baldwin (2006) has argued that the bilateral FTA strategy is likely to trigger a domino effect of trade liberalisation. Countries that are excluded from either a

³ A similar interpretation can be made for the case of South Korea-Chile.

regional or bilateral FTA will feel the effect of trade diversion. Therefore, the excluded countries will seek to pursue FTA negotiations to level the playing field, to minimise these economic losses and, possibly, to maximise economic gains for its pro-free-trade domestic actors in the short run once these FTAs are achieved (ibid.: 1467–1468).

Japan decided to conduct FTA negotiations in order to reduce eventual losses from not having an FTA with Chile. According to Japanese trade ministry negotiators:

Japanese businesses have complained about disadvantages in competing with the country's FTA partners in the Chilean market and urged the government to speedily sign the pact. (JT 2006)

The main threat posed by these FTAs was to the auto-industry and electronic products; these were entering Chile without tariffs from the US, South Korea, the EU and especially China, whereas Japanese products still carry a six percent tariff. Although Japanese autos dominate the Chilean market, the eventual loss of a share of the market due to China's new auto exports at low prices could reduce the economic gains of Japanese producers. In addition, Chinese electronic products, for example laptops, DVD players, digital cameras, mobile phones, printers and other technological devices automatically became tariff-free once the FTA was implemented (Direcon 2006: 2).

The fact that Chile could become an access point in the near future for more attractive economic markets such as the Common Market of the South (MERCOSUR) is another factor that facilitated a final agreement (Nippon Keidaren 2000). This possibility served as an extra stimulus for Japanese business groups to lobby their government in order to conclude an FTA with Chile. The other countries that have an FTA with Chile have also special interests in broadening their economic influence in the rest of South America, specially China (Fuentes 2006: 112). The Japanese pro-FTA groups were concerned that the trade diversion could go beyond the Chilean market and threaten its position in the rest of South America.

Furthermore, China, Korea [Republic of Korea], and other countries have stepped up their efforts to conclude EPAs and FTAs, turning them into arenas of international competition. (Nippon Keidanren 2006)

Therefore, the FTA between these countries was motivated by the loss-aversion behaviour of important Japanese domestic groups, which saw how their main competitors from other countries were getting preferential positions in the

Chilean market. Autos and copper dominated the agenda in this FTA negotiation not only because they are the main source exports for Japan (autos) and Chile (copper) but also because of the growing web of FTAs that Chile has achieved, which threatened the dominant position of Japanese auto-exporters and electronic device producers.

Most importantly, high METI⁴ officials convinced that to prevent a repetition of the experience of Japanese firms in Mexico in other countries, Japan would have to pursue FTAs proactively. (Manger 2005: 817)

The Final Outcome beyond the Agriculture Issue

The FTA between Japan and Chile can be classified as a last-generation FTA agreement or WTO plus, despite the exclusions of agricultural, seafood, dairy and some sugar products, because the scope of this FTA goes beyond the extant WTO standards. This FTA includes provisions such as trade facilitation, competition policy, public procurement, investment cooperation, property rights, temporary entry of persons, rules of origin, and a cooperation agreement on the environment. The inclusion of these issues responds to the need of these two countries to provide more comprehensive and accessible mechanisms of governance to their economic actors in world economic affairs (cf. MOFA 2007).

Moreover, it seems that the negotiation of these issues in bilateral FTAs can facilitate their inclusion into the WTO agenda if the negotiations at this level are eventually broken through. FTAs – such as the one between Chile and Japan – are not made in a vacuum. On the contrary they are part of a multilevel strategy of rule-making (Woolcock 2006: 242). Economic negotiations are thus no longer confined to trade barriers (tariffs and quotas), as was the case from the 1960s to the 1980s, but are becoming more and more about non-trade barriers encompassed in domestic laws (Landau 2000: 6). Nevertheless, these mechanisms of economic governance were included to facilitate the trade creation process between the parties in traditional areas of goods and services. It is thus expected that the extant FTA between these countries will boost trade from the first year of its implementation since the FTA lifted tariffs from the first day of its implementation on 70 percent of Chile's total exports to Japan and 90 percent of Japan's total exports to Chile (Prochile 2006).

⁴ METI is the abbreviation of Japan's Ministry of Economy, Trade and Industry.

Conclusion

The negotiated outcome of the FTA between Japan and Chile provides rule-binding mechanisms of governance to both countries. At odds, the WTO plus issues did not pose any trouble to the negotiators, even the ones of property rights and rules of origin that a priori can be perceived as difficult to solve when an industrialised country negotiates an FTA with a developing one.

In fact, the Japanese FTA strategy towards Chile was dominated by concerns on potential losses for the agricultural sector if many concessions were given because of Chile's comparative advantages on this issue area. However, Japan's trade strategy once again passed the test of negotiating with an agricultural country.

The rapid agreement reached in five rounds despite the sensitive products concentrated in the agricultural sector was facilitated by choosing a defensive distributive strategy which was reciprocated by Chile (exclusion by exclusion). Moreover, Japan made clear to Chile, at the outset of the negotiation, its non-negotiable products. Yet Japan's success was also in part determined by Chile's FTA policy, which is characterised by its pragmatism and flexibility to accommodate the counterpart's demands, whenever the success of the negotiation is at stake and when the counterpart has a significant economic market.

In addition, external elements also influenced the need to reach a rapid agreement. The fear of Japanese business groups of being displaced in some markets by their main competitors' proactive FTA policy played a decisive role not only in launching the FTA negotiation with Chile but also in reaching a rapid agreement. The main perceived economic concern for Japan is the growing economic influence of China. This latter country is starting to pursue a proactive trade agenda in which bilateralisation is a key component in its intra-regional and inter-regional economic relations. Proof of this policy is China's first FTA with Chile.

The FTA between Japan and Chile opens the possibility of creating trade beyond the extant dominant trade pattern of Japanese autos and electronic articles for Chilean minerals. Whether the domestic actors of both countries take advantage of this new opportunity to maximise economic gains is something that has to be assessed in the future. What is clear is that Japan has learned to balance the need of pursuing FTAs to satisfy its business groups without causing excessive pain to its agricultural sector, especially when the predominant trade

pattern is marked by a North-South division like the economic relation between Japan and Chile.

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